QUALIFYING AND MAINTAINING TAX EXEMPT STATUS

HOW TO ACHIEVE TAX EXEMPT STATUS FOR YOUR ORGANIZATIN AND MAKE SURE IT STAYS THAT WAY

By: Jeffrey A. Slavin, Esq.

Businesses everywhere enjoy the benefits of a tax-exempt status; does your business qualify? Qualifying groups are free from tax on federal, state and local levels, which allows these entities to devote a larger proportion of resources to achieving their true altruistic goals. Their status as "tax-exempt" can also qualify groups for special grants, funding and even special rates on postage. Furthermore, donors generally prefer contributions to these groups because they can deduct gifts from their own income taxes.

This article will focus on two common forms of tax-exempt businesses, the 501C (6) Business League and the 501C (3) Educational Organization, but the principles may be applied elsewhere.

Achieving Tax-Exempt Status

Four qualifications must be met in order for one's business to achieve the status of a 501C (6) Business League. First, its activities must be devoted to promoting business conditions in one or more lines of business. Second, the league must show that conditions of a particular trade or interest of the community will be advanced by its existence. Third, no part of net earnings may go toward the benefit of any private shareholder or individual. And finally, there must be meaningful membership support.

Similarly, a 501C (3) Educational Organization must be true to its function. It must conduct activities devoted to promoting an educational purpose. Next, just as in the Business League, no part of net earnings may inure to the benefit of any private shareholder or individual. Finally, the organization may not be an "action organization." In other words, it cannot exist to influence legislation or engage in campaign activities.

Don't Lose Your Status!

Losing tax-exempt status can often prove fatal for charitable organizations. The imposition of back taxes, penalties and the abeyance of an income stream are more than likely too much to recover from for most organizations. Therefore, a watchful eye on risky behavior is paramount for any chartable leader.

There are five separate and important ways a Business League can lose its tax-exempt status. The first is cessation of purpose. A Business League must always be devoted to promoting its particular business conditions. Next, no part of the organizations net earnings may inure to the benefit of its members. This can include providing financial assistance or welfare to its members, paying member expenses or even leasing office space rent free. Third, a league must never carry on a for-profit business. Fourth, the organization must never perform particular services for individual persons. These services can range from advertising to operating parking lots for members' customers. Last, but certainly not least, a Business League must always remember to file its annual return with the IRS. This unsurreptitious mistake can happen to well-meaning, yet disorganized groups.

Educational Organizations exist with equal risk of losing their tax-exempt status and must be aware of the hazards. An Educational Organization must look to avoid the same pitfalls of a Business League – cessation of purpose, inurnment of earnings, benefiting private interests – but must also watch for political participation.

The existence of non-profit, tax-exempt organizations play an important and necessarily role in our society. We rely on these groups to take up the full-time task of improving a world in which most individuals feel bereft of time and focus to make a difference. In the vast majority of circumstances, tax-exempt groups must maintain their status in order to function. The imposition of back-tax assessments and penalties for losing their status, coupled with the impending possibility of charitable deductions being wiped from our taxing lexicon, will most likely impose too much of a hardship for groups to carry on. Therefore, I implore you to look at your organizations and make sure they continue to remain organized and in compliance.

ABOUT THE AUTHOR

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